Vornado®, INC. report

for the five month fiscal year ended January 31, 1964

TO OUR STOCKHOLDERS:

We are pleased to submit our audited financial statements for the five month period ended January 31, 1964.

This interim report conforms with the decision to change the end of our fiscal year from August 31 to January 31. The January 31 fiscal year will permit a comparison of our operation with others in the retail industry. Our financial condition would also be available after the close of our peak selling season. The change in our fiscal year ending was approved by our stockholders at our last annual meeting held January 14, 1964.

No comparative figures have been included as there was no audit for the comparable period a year ago.

Sales and Earnings

Sales for the five months, including leased departments, amounted to \$80,080,451. Net earnings, after federal income taxes of \$1,550,000, were \$1,785,670, equal to \$1.36 per share on the 1,310,593 shares of common stock outstanding. Federal income taxes were provided for at the effective rate of 46.4%.

As a matter of interest, unaudited sales, including leased departments, for the five months ended January 31, 1963 were \$70,072,859 so that sales for the five months were approximately 15% ahead of a year ago.

This rising trend was accentuated in February and March 1964 when sales for the two months amounted to \$24,499,000 compared with sales of \$18,830,000 in the same two months last year, a gain of 30.1%.

Comparison of Previous Years

In order that our stockholders may have a basis for comparison, your company has estimated sales and earnings for the two twelve month periods ended January 31, 1964 and January 31, 1963 using full taxes at present rates. These estimations show that for the 12 month period ended January 31, 1964 sales, including leased departments, amounted to \$164,777,000 and net earnings were \$2,708,000, equal to \$2.06 per share on the 1,310,593 shares outstanding. For the previous year which ended January 31, 1963, sales, including leased departments, amounted to \$134,059,000 and net earnings were \$2,226,000, equal to \$1.70 per share on the like number of shares. Sales in fiscal 1964 were 22% higher than in the previous year and earnings after taxes were up 21%.

A more complete report will be made to the stockholders for the fiscal year ending January 31, 1965.

HERBERT HUBSCHMAN
Chairman of the Board

MURRAY J. SIEGEL
President

Vornado®, INC. a Kansas corporation **AND SUBSIDIARIES**

STATEMENT OF CONSOLIDATED EARNINGS

Five Months Ended January 31, 1964

Net sales, including leased departments	$80,080,451
NET REVENUES:	
Net sales, exclusive of leased departments	74,592,096
Other operating revenues, less allocated expenses	542,266
TOTAL NET REVENUES	75,134,362
Cost of sales, operating and administrative expenses	71,428,948
PROFIT FROM OPERATIONS	3,705,414
OTHER CHARGES, NET:	
Interest and debt expense	481,633
Other income, net	111,888
	369,745
EARNINGS BEFORE PROVISION FOR FEDERAL INCOME TAXES	3,335,669
PROVISION FOR FEDERAL INCOME TAXES (note 4)	1,550,000
NET EARNINGS	$ 1,785,669

Depreciation and charges in lieu thereof on property and equipment amounted to $818,656

STATEMENT OF CONSOLIDATED RETAINED EARNINGS

Five Months Ended January 31, 1964

Balance at beginning of period	$ 6,528,536
Net earnings for the period	1,785,669
Balance at end of period	$ 8,314,205

See accompanying notes to consolidated financial statements.

VORNADO, INC. a Kansas corporation **AND SUBSIDIARIES**

Consolidated Balance Sheet

January 31, 1964

ASSETS

CURRENT ASSETS:	
Cash	$ 6,816,908
Receivables:	
Trade	1,506,145
Other	120,514
TOTAL RECEIVABLES	1,626,659
Merchandise inventory, at lower of cost (first-in, first-out) or realizable market	25,698,097
Prepaid expenses	296,572
TOTAL CURRENT ASSETS	34,438,236
OTHER ASSETS:	
Mortgages receivable, less installments due within one year and reserve (note 3)	2,343,476
Rent, utility and other deposits (notes 3 and 7)	932,023
Miscellaneous	305,234
	3,580,733
Property and equipment, at cost (notes 2, 3, 4 and 5):	
Land, parking areas and buildings	12,989,329
Furniture, equipment and leasehold improvements and costs	12,123,875
Construction in progress	3,315
	25,116,519
Less accumulated depreciation and amortization	5,323,220
NET PROPERTY AND EQUIPMENT	19,793,299
Cost of leases and occupancy rights, less accumulated amortization of $560,529 (note 4)	1,247,671
Debt discount and expense	1,089,092
	$60,149,031

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

January 31, 1964

LIABILITIES	
CURRENT LIABILITIES:	
Notes payable	$ 2,064,637
Long-term debt installments due in one year	1,307,571
Accounts payable, trade	12,422,829
Federal income taxes, estimated (note 4)	1,662,273
Other, including accruals	1,735,399
TOTAL CURRENT LIABILITIES	19,192,709
Leased department rental and other security deposits	363,658
LONG-TERM DEBT (note 5):	
5% Convertible Subordinated Debentures	5,237,000
3.10% Junior Subordinated Note	2,259,000
Other	9,689,534
	17,185,534
Less installments due within one year	1,307,571
TOTAL LONG-TERM DEBT	15,877,963
Deferred Federal income tax (note 4)	292,530
STOCKHOLDERS' EQUITY	
Common stock of 10¢ par value per share. Authorized 2,500,000 shares; issued and outstanding, including treasury shares, 1,317,593 (note 6)	131,759
Additional paid-in capital (including capital arising in reorganization)	16,046,207
Retained earnings (note 5)	8,314,205
	24,492,171
Less cost of 7,000 shares of common stock held in treasury	70,000
TOTAL STOCKHOLDERS' EQUITY	24,422,171
Contingent liabilities and commitments (notes 2, 4 and 7)	
	$60,149,031

See accompanying notes to consolidated financial statements.

Vornado®, INC. a Kansas corporation **AND SUBSIDIARIES**

SUMMARY OF CHANGES IN WORKING CAPITAL

Five Months Ended January 31, 1964

Source of funds:	
Net earnings	$1,785,669
Add non-cash items charged to earnings:	
Depreciation and amortization of property and equipment, including charge in lieu of depreciation	818,656
Amortization of cost of leases and occupancy rights and debt discount and expense	190,131
Investment credit	212,130
Total from operations	3,006,586
Sales of properties under leaseback agreements	3,900,000
Other	43,773
	$6,950,359
Application of funds:	
Additions to property and equipment	$3,075,451
Decrease in long-term debt not due within one year	274,685
Other	379,351
	3,729,487
Increase in working capital	3,220,872
	$6,950,359

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

January 31, 1964

(1) Change of fiscal year:

The fiscal year of the Company and its subsidiaries has been changed to end on January 31; formerly the fiscal year ended on August 31. The change was made to conform the financial reporting year with the Company and industry natural business year. Because of the seasonal nature of the Company's sales activity, the results of operations for the five months ended January 31, 1964 may not necessarily reflect a proportionate share of the earnings for a full year.

(2) Long-term leases:

During the five months ended January 31, 1964, the Company sold at approximate cost and leased back two of its stores at annual rentals of $296,000 which rents were calculated to amortize the debt of the lessor (cost of the properties) including interest, over the twenty-five year term of the leases. In addition, subsequent to January 31, 1964 the Company entered into a similar sale and leaseback transaction for another of its store properties at an annual rental of $130,000.

Substantially all of the leases covering certain of the Company's stores, warehouses and other properties, including those mentioned above, are for terms in excess of three years. Average annual rentals during the next five years, exclusive of taxes, insurance and maintenance, approximate $1,925,000 per annum.

(3) Mortgages receivable:

Mortgages receivable, net of installments due within one year and bearing interest at rates of 5% and 6% per annum are as follows:

Affiliated co-partnerships	$3,820,886
Held by others	519,288
	4,340,174
Less reserve	1,996,698
Net mortgages receivable	$2,343,476

The mortgage balances result primarily from three sale and leaseback transactions with an officer and affiliated co-partnerships during 1961. The selling price of these properties (satisfied in part by purchase money mortgages providing for amortization to commence in five years) was $1,609,898 in excess of the depreciated cost. As the terms of the sales and leasebacks provide repurchase options during the five years 1966 to 1971 at the original selling prices, the excess has been applied as a reserve against the face amount of the mortgages receivable. Also, an additional reserve is being provided by an annual charge to earnings which is equivalent to the depreciation, net of future tax benefit, that would have been provided on such properties had they not been sold. Should the properties be repurchased the charge in lieu of depreciation will be included in the accumulated depreciation accounts or will provide a means of equalizing annual rentals should the properties not be repurchased.

These properties were leased back in 1961 for periods of twenty and twenty-five years at annual rentals (exclusive of taxes, insurance, maintenance, etc.) of $495,000 for the first five years and $745,000, $970,000, $1,195,000 and $920,000, respectively, for each of the succeeding five-year periods. The leases also provide for the payment of security deposits of approximately $950,000 during the next five years which amount approximates the amortization payments on mortgage debt assumed by the lessor during such period.

(4) Federal income taxes:

The provision for Federal income taxes includes a tax reduction of $122,000 resulting from the difference between the amortizable value of occupancy rights and leases for tax and financial statement purposes and represents a permanent tax benefit. In addition, a temporary tax advantage results from the use of a tax amortization period which is shorter than that used for financial statement purposes. The provision for Federal income taxes includes an amount for taxes temporarily so deferred and is reduced by the expected future tax benefit in connection with the charge in lieu of depreciation mentioned in Note 3.

The utilization of net operating losses incurred by the Company prior to its merger with Two Guys From Harrison Inc., resulted in aggregate tax reductions of $4,706,000 in prior periods and is subject to review by the Internal Revenue Service.

The investment credit applied as a reduction of taxes payable, in the amount of $215,000, is being taken into income over the lives of the related property. The unused investment credit available for the reduction of future taxes payable is approximately $48,000.

(5) Long-term debt:

The 5% Convertible Subordinated Debentures are due March 1, 1982 and are convertible into shares of common stock of the Company at a conversion price per share of $37.00 if converted prior to March 1, 1965, and at an increasing price thereafter. Mandatory annual sinking fund payments of $100,000 commence on March 1, 1968, for a period of five years and thereafter at the rate of 10% of the principal amount outstanding on September 1, 1972. The principal amount of debentures converted subsequent to September 1, 1967, may, subject to some limitations, be applied in reduction of the sinking fund obligations due thereafter. The debentures may be redeemed at gradually decreasing redemption prices ranging from approximately 105% of principal amount to face amount after February 28, 1981.

The 3.10% Junior Subordinated Note due May 1, 1976 provides for annual fixed sinking fund payments, which commenced May 1, 1962, in the amount of $40,000 and in increasing annual amounts to $59,000 due on May 1, 1975, with the balance of $1,660,000 payable on May 1, 1976. The note contains prepayment and repurchase provisions.

The Company has in effect a term-loan agreement expiring September 17, 1964, the purpose of which is to provide temporary financing of the Company's construction program. Basically the agreement provides for revolving credit of up to $5,000,000 for the purpose of acquiring land, buildings and improvements. The terms provide for payment over a maximum period of five years, interest rates to 6%, commitment fees, prepayment privileges, etc. At January 31, 1964 no borrowings were outstanding under this agreement.

Other long-term debt of the Company and its subsidiaries consists of first and second mortgages on real property, notes payable secured by conditional sales contracts on equipment and notes payable to banks and others at interest rates varying between 4½ and 10%.

Under the terms of the various loan agreements, the Company is subject to restrictions relating to working capital, payment of dividends (other than stock dividends), acquisition of its capital stock and other customary restrictions. Under the most restrictive terms, including those contained in the term-loan agreement, the Company must maintain a minimum consolidated working capital of at least $8,500,000 and limit dividend payments (other than stock dividends) and other distributions on or purchases of capital stock during each fiscal year to 25% of its consolidated net earnings for the previous fiscal year. At January 31, 1964, approximately $450,000 of consolidated retained earnings was free of such restrictions.

The book value of property pledged under mortgages, conditional sales contracts and notes secured by trust receipts amounted to approximately $11,170,000 at January 31, 1964.

(6) Stock options and warrants:

As of January 31, 1964, shares of stock were reserved for warrants, options, conversions, etc., as follows:

Description			*No. of shares*
Purchase warrant at $16.00 per share, exercisable only in its entirety and expires on April 27, 1967			42,000
Stock options to officers and key employees:			
Option price	*Expiration date*	*Shares presently exercisable*	
$15.57	Mar. 1, 1971	20,000	30,000
15.57	May 8, 1972	1,600	8,000
19.06	Jan. 1, 1973	6,666	20,000
20.15	Mar. 1, 1966	10,000	15,000
20.77	Mar. 1, 1968	—	10,000
22.07	Jan. 1, 1968	8,334	25,000
27.60	May 8, 1972	15,050	75,250
		61,650	183,250
(No options were exercised during the five months ended January 31, 1964)			
Reserved for conversion of 5% Convertible Subordinated Debentures			141,541
			366,791

On February 6, 1964 the Board of Directors cancelled all options at $27.60 and granted in place thereof qualified stock options at a price of $19.00 per share (100% of the fair market value on that date), exercisable as to 60% of the shares on or after June 10, 1965, an additional 20% on or after June 10, 1966 and all of the shares on or after June 10, 1967. The options expire February 1, 1969. The granting is subject to approval by the stockholders. On April 9, 1964, additional qualified options on 16,250 shares were granted at $23.32 (100% of the fair market value on that date) subject to the same approval, exercise rights and expiration as the above shares.

By agreement dated November 15, 1963 the former president of the Company surrendered options on 25,000 shares held by him, and among other things agreed not to compete with the Company for a period of six years during which time he will receive monthly payments of $4,687.

(7) Contingent liabilities and commitments:

Guarantees:

The Company is contingently liable for payments under certain mortgages relating to properties sold under sale and lease-back transactions in prior years. As of January 31, 1964, such mortgages had unpaid balances of approximately $1,908,000. In the case of one such mortgage, U.S. Government securities of a par value of $76,000 have been deposited as security for the payment thereof. In the opinion of management, the possibility of any loss related to these mortgages is extremely remote.

Litigation:

The Company and other retailers have been for some years, and are currently engaged in litigation involving Sunday "blue law" statutes. Such statutes presently prohibit the Company from selling a substantial portion of its merchandise on Sunday.

ACCOUNTANTS' REPORT

Peat, Marwick, Mitchell & Co.
Certified Public Accountants
1180 Raymond Boulevard
Newark 2, N. J.

To the Stockholders and Board of Directors
Vornado, Inc.:

We have examined the consolidated balance sheet of Vornado, Inc. (a Kansas corporation) and subsidiaries as of January 31, 1964 and the related statements of consolidated earnings and retained earnings for the five months then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, subject to the final determination of the net operating loss carryforward as an offset against taxable earnings in prior years (see note 4 of Notes to Consolidated Financial Statements), the accompanying consolidated balance sheet and related statements of consolidated earnings and retained earnings present fairly the consolidated financial position of Vornado, Inc. and subsidiaries at January 31, 1964 and the consolidated results of their operations for the five months then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Also, in our opinion, the accompanying summary of changes in working capital presents fairly the information shown therein.

Peat, Marwick, Mitchell & Co.

Newark, N. J.
April 15, 1964

Vornado 1964